RICHARD RUSSELL'S **DOW THEORY LETTERS, INC.**

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April 25, 1979 **LETTER 755**

April 12, DJIA 870.50; PTI 974; A-D Ratio –18.63
April 20, DJIA 856.98; PTI 966; A-D Ratio –19.03

POLICY: My policy during 1979 is expressed in one word: **liquidity**. What is liquidity? Liquidity is cash or the nearest thing to it. Since cash in the mattress doesn't pay us a yield and the safest US "paper" does, I have been recommending 91-day Treasury bills. These first obligations of the US Government provide a return (free from state taxes) of 9.6%. They can be purchased or sold any time in any quantity, no matter how large, and they are outside the banking system. On a risk to return basis, T-bills make more sense to me here than anything else. If you had stayed in T-bills over the last six months you would have outperformed just about everything from stocks to Swiss francs to bonds to gold. SO, sit tight with your T-bills until the atmosphere clears. So far, there's still a dense smog over the world of securities, as far as this writer is concerned.

THE PICTURE: Sometimes the biggest and the most fundamental picture is the most difficult one to see. For instance, since the depths of the Great Depression in 1932 there have been nine major expansions in the economy and eight major recessions. During each successive economic expansion since 1932 both the D-J Industrial Average and the Standard & Poor's 500 Composite have recorded a new historic high–with the single exception of the expansion which began in 1974. The economy went into recession during 1974-75, then turned up during late-1975. But in the period of the economic expansion since 1975 neither the Dow nor the S&P 500 has been able to record a new high.

"What is the market trying to tell us," I ask myself. "Why should this be the first instance since 1932 in which the major Averages have failed to go to new highs?" My own feeling is that the market is making a statement. It is telling us that there is something "wrong" with corporate earnings, as stated. And it is also telling us that there is something drastically wrong with the US economy.

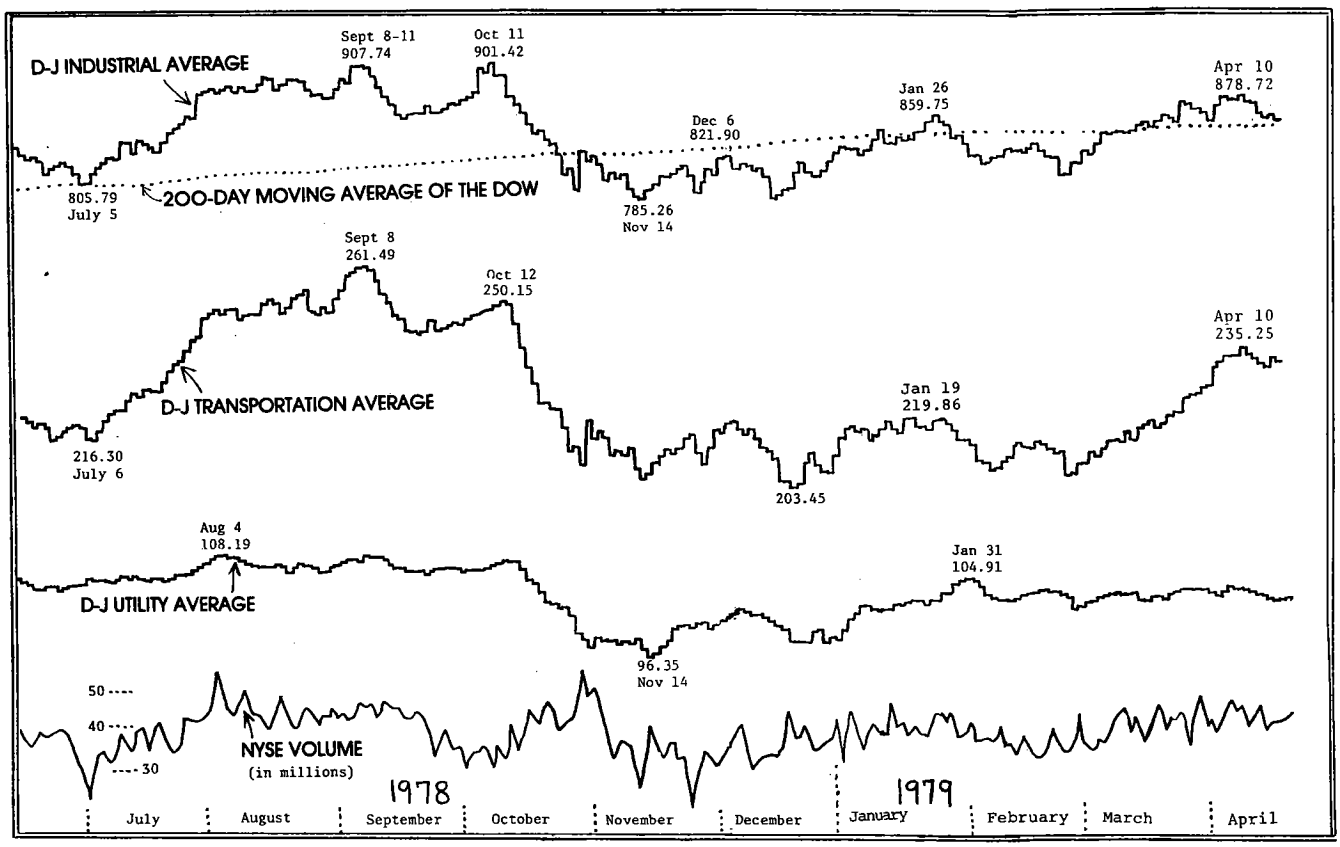
I have taken a section of this Letter to explain what is wrong with corporate earnings. And as far as the economy is concerned, the current expansion is basically flawed ("sick" would be a better word for it) because it is built on a structure of debt and inflation. The inflation has caused consumers to "buy before it all goes higher" and to abandon their normally conservative reaction to higher prices. The easy access to money has tempted corporations to "borrow now before interest rates go higher." Thus, much of this extended expansion in the economy has been underwritten by FEAR rather than confidence.

Furthermore, it is taking more and more debt to produce less and less GNP. Last week the US passed a milestone in that the Federal debt hit the **$800 billion** mark for the first time in history. The interest on the Federal debt (see insert at right) was $24 billion for the current fiscal

U.S. FINANCES

WASHINGTON (AP) — Here are the figures on government spending and debt (last six digits are omitted) as of April 17: ←

Total public debt	804,452
Interest on public debt for Feb.	4,320
Interest for fiscal year through Feb.	24,537
Budget deficit for Feb.	5,100
Budget deficit for Feb. last year	6,997
Budget deficit fiscal year so far	31,599
Estimated deficit fiscal 1979	33,175
Outlays fiscal year so far	202,052
Outlays same period year before	184,138
Gold for Feb.	11,544



year so far). My guess is that interest charges for the entire fiscal year will be near the $60 billion mark. Thus, Federal debt and interest costs are running out-of-control.

Conclusion: My conclusion is that the Averages, in their refusal to record new highs during this economic expansion period, are issuing us a warning. They are telling us that since they produced a weak upside performance during the current expansion, they are going to produce a strong **downside** performance during or prior to the next economic contraction.

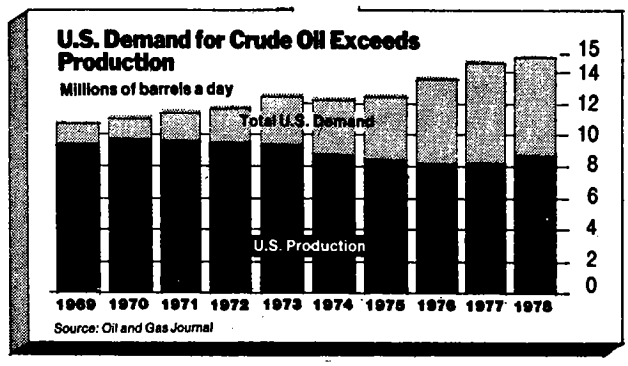
But I feel that the period of the next economic trouble could be some ways off. It is possible that there is currently too much pessimism, too much fear, too much concern. At any rate, this is the time to be patient and let the market do the talking. I don't think the market is going to be kind to those who jump the gun this time. Certainly the market has been kind to very few so far this year.

It is most fascinating to note that the gambling stocks have been the darlings of 1979. I believe that gambling is the reverse side of the fear-coin:fear on the one side, gambling on the other. Today's public is fearful; they don't know how they are going to make ends meet. Inflation is robbing the average citizen of his buying power and savings, and taxes are robbing him of his income. The resultant fear regarding his ability to survive is breeding a "what the hell" attitude. One expression of that attitude is gambling. "It's no use trying to save," reasons the citizen, "so why not have fun with my money and maybe double or triple it. If I lose it, who cares, they're going to steal it from me anyway." That's the way many Americans are thinking, and that's the reverse side of the fear-coin–gambling; make it quick, and if you lose it, so what!

THE MARKET: This is one of the most interesting market periods I have ever had to deal with. The only thing obvious about it is that there is great confusion. Predictions and forecasts are a dime a dozen. Some analysts are convinced that we are still in a bull market that began in 1974. Others are convinced that the bull market ended in mid-1976. Still others are of the opinion that everything since 1975 was simply part of a huge bear market correction (as per 1930) and that before long we will be testing the 1974 lows.

Personally, I feel that this is a time to have a totally open mind about the situation. At any time in the past 100 years one could have said that "This is a truly different situation." But today I believe that phrase can be made with true conviction. Consider this: The phenomenal growth of the US has always been accompanied by three trends: (1) vast almost unlimited natural resources, (2) unlimited land and an ever-expanding frontier, and (3) virtually unlimited access to cheap energy.

Today all three of those trends have ended. The US today is dependent on the rest of the world for an increasing number of minerals and metals. The "way West" has ended, and the new frontiers and cheap land are now no more (or very, very limited). Cheap energy is history, and this chart graphically explains why. Thus, investors in the US truly face new conditions today.



It should never be forgotten, however, that the market looks ahead not with two or ten or a thousand eyes, but the market looks ahead with millions of eyes. And the market sees clearer and farther than any man or group of men. Therefore, I am telling subscribers that it will be absolutely crucial to follow the market itself during the period ahead.

Right now, I see four major puzzles in the market. (1) The market has now advanced or at least held up for almost 55 months following the 1974 lows.

Since World War II the market has never gone more than 52 months without producing a dramatic and drastic cyclical low. Thus, in terms of timing, we have witnessed something new.

(2) While the foregoing observation might seem to be an indication of strength, it is nevertheless true that the Averages have refused to advance to new highs during this economic expansion. This has not happened on any expansion since 1932, and that would seem to be a sign of long-term weakness (unless, of course, we are fated to see new highs in the Averages in the period ahead).

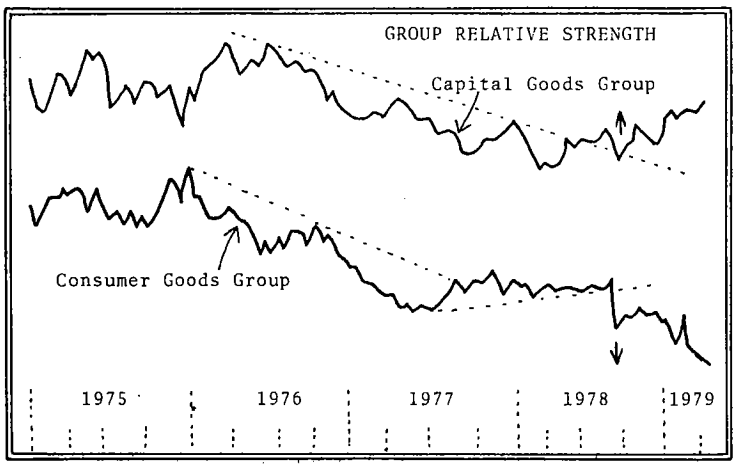
(3) The odd-lot public has been selling stock at an *unprecedented* rate for the past three years. In fact the average selling ratio has been 216, which means that for every 100 odd-lot shares purchased, 216 have been sold. This is the heaviest rate of odd-lot selling seen in the 60 year history of these statistics. Strangely, the odd lotters have a good record of selling heavily near the extreme highs in price and buying near the major market bottoms.

Yet some analysts feel that the record odd lot selling during the past three years is going to prove to be misguided, and that this fear-selling portends much higher markets. Personally, I am of the opinion that the public is strapped for cash and is now opting for INCOME. This would account for the tremendous sales of common stocks and the large purchases of bonds, bond funds, T-bills and money instruments.

Ned Davis of J. C. Bradford believes that we won't see heavy public buying of common stocks until stock yields once again surpass bond yields. At any rate, it is interesting to note that the public still owns 70% of all common stock, even after their three-year selling spree. So there's a lot more stock in the hands of the public that could be sold. And the mystery of the amazing odd-lot selling goes on.

(4) As of April 14 the "Big Block" ratio (5-week basis) hit a record high of 49%. This is the ratio of up-ticks to down-ticks in the big (over 25,000 shares) NYSE blocks (these blocks are traded by the institutions). What this very high ratio shows is white-hot enthusiasm on the part of the institutional managers. The history of this ratio shows that it usually hits peaks near highs in the market (which obviously doesn't say much for institutional timing). When you put the big block record peak together with the record rate of odd-lot selling, it makes you wonder. It makes you wonder if this market isn't very close to an important top.

Maybe I should label this puzzle No. 5 or maybe I should call it an observation. The accompanying chart shows the relative strength of two major S&P stock groups, Capital Goods and Consumer Goods. I keep this chart on a weekly basis (relative strength of the two groups compared with the NYSE 400 Industrial Average).



Note that the Consumer Group was declining in RS during 1976 and part of 1977. Consumer RS turned up mildly during mid-1977 and remained up until mid-1978. From there on, the Consumer Group was bearish. Over the same period the Capital Goods Group remained steadfastly bearish, but during the third quarter of 1978 Capital Goods turned bullish on a relative strength basis.

Does this mean that as the consumer segment of the economy turns soft, the capital goods sector is going to turn rosy? The market, at any rate, is telling us that capital goods stocks are now definitely outperforming consumer goods equities. Conclusion: if a recession is to be held off or put off from here, it will be due to strength in capital goods buying, rather than buying on the part of consumers. I would therefore expect consumer stocks (hotel, leisure time, radio-TV, publishing, mobile homes, restaurants) to act poorly, while capital goods stocks (coal, steel, chemicals, oils, paper, metals, machine construction) continue to outperform the market.

* *

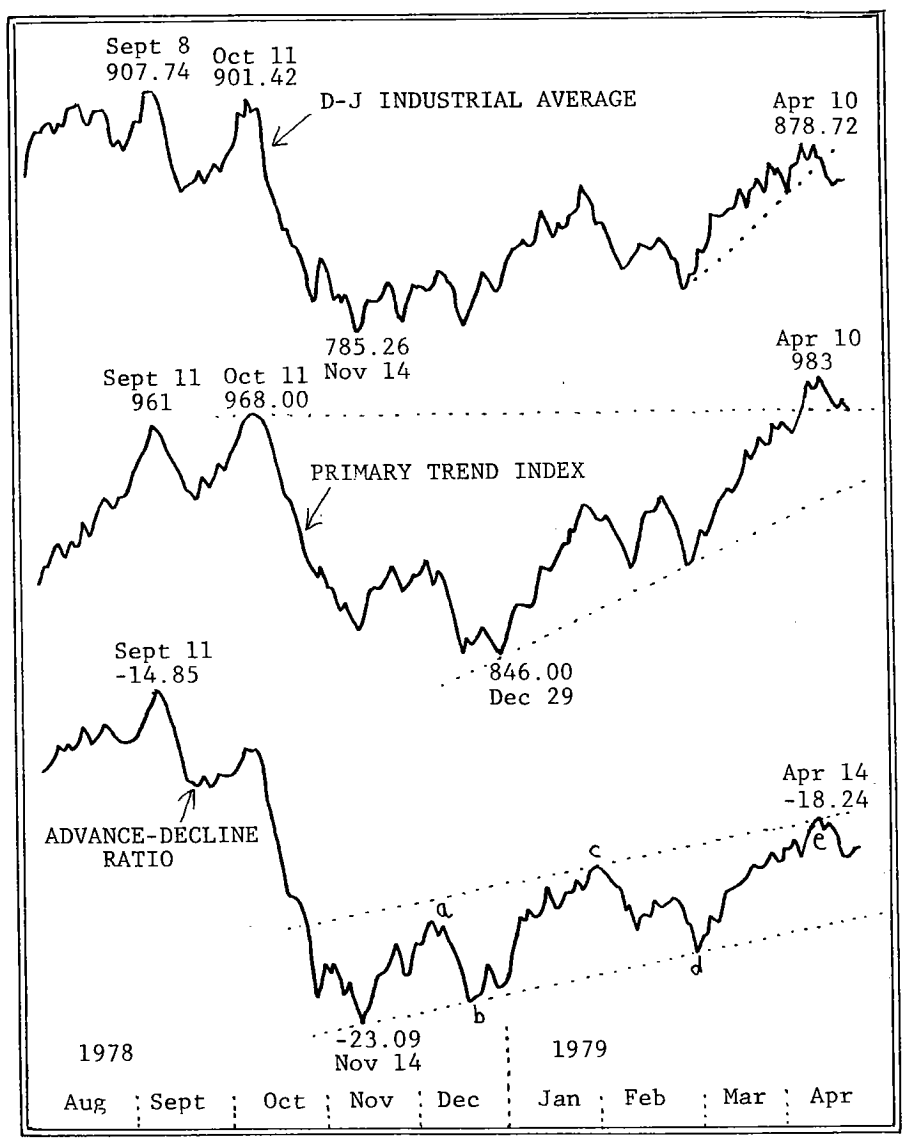
From the standpoint of Dow's Theory, the Averages have not done anything particularly important since the last mailing. When Industrials bettered the January peak of 859.75 confirmed by a Transport bettering of 219.86 the secondary trend of the market turned bullish. Many analysts enthusiastically labeled this move a "primary bull signal." I don't go along with that rosy interpretation, however.

On April 10 Industrials recorded a peak of 878.72 while Transports on the same day hit 235.25. A sharp little decline followed. Since (in retrospect) any decline may be the start of something bigger, it will be well to watch the April 10 highs. My earlier "prediction" of an early-May top in the market and a major July low now seems to have gained general acceptance, and many analysts are joining in on the May-to-July chorus. This makes my scenario a bit suspect, and I wonder if April 10 might not have been a secondary top.

Now turn to the daily chart of the Primary Trend Index (PTI) and the A-D ratio. In the last Letter I said that the action of the PTI may well be our best indicator of what lies ahead. A rising PTI acts as a rising floor under the market. There is no way for the PTI to rise *persistently* without taking the general market up with it. Conversely, a steadily declining PTI must take the market down with it.

In view of that, let's study the accompanying chart. The PTI turned up from the 846 level on December 29. On April 10 the PTI (having bettered the October 11 peak of 968) recorded a high of 983. This new high was not confirmed by the Dow (the Dow failed to better its late-1978 peak of 907.74). This tells us that price (the Dow) has so far refused to confirm the technical syndrome (the PTI).

From this point on, the PTI must be watched carefully. If the PTI now works above its peak (above 983) and pushes up from there, I would expect the Dow and the rest of the market to follow. BUT, if 983 proves to be the peak for the PTI and this indicator then trends steadily down. it will be a strong indication that the market is moving into the trouble area.



We are building an interesting and perhaps very significant DIVERGENCE between the Dow and the PTI. Note the series of lower peaks in the Dow: 907.74 (Sept. 8), 901.42 (Oct. 11), 878.72 (April 10). Against this we have a series of rising peaks in the PTI: 961 (Sept. 11), 968 (Oct. 11), 983 (April 10). Divergences of this kind can be very tricky and difficult. This divergence, as I see it, is telling us that regardless of technical strength (as exhibited by the PTI) the price (Dow) has refused to respond. I feel that there is a limit to how far the PTI can rally without Dow confirmation. If the Dow cannot move up and out by mid-May, I would expect important trouble!

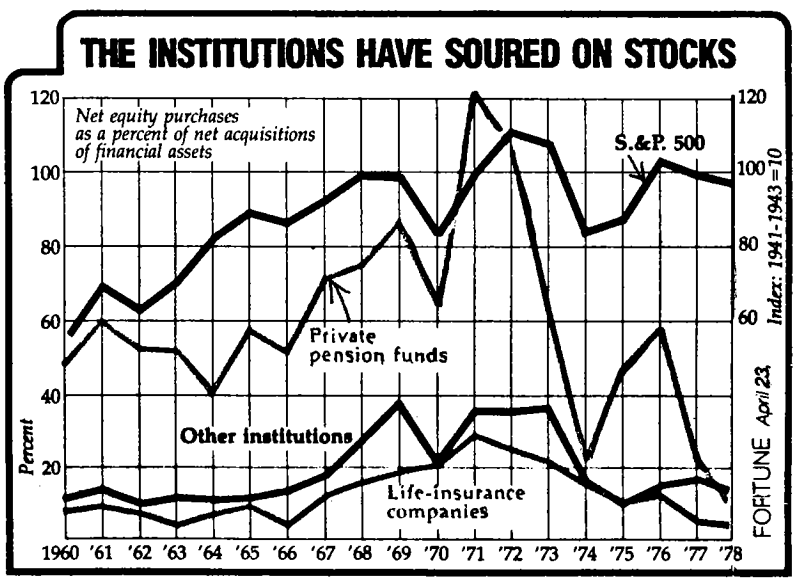
At the bottom of the chart we see the A-D ratio, an index which acts as an unweighted average of the entire NYSE. The picture here is not particularly impressive. Between September 11 and November 14 the A-D lost a whopping 8.24 points. On the recovery from the November 14 low the A-D has regained (so far) about 58% of its previous losses. Against this the Dow (at 878.72) has recouped 67% of its September-November losses.

Note that the A-D from its November 14 low has traced an a-b-c-d-e pattern of rising waves. Such patterns are often completed at the end of the e-wave. At any rate, what is clear is that the A-D is now lagging the Dow and the Dow in turn is lagging the PTI.

Conclusion: The story will be told by the Dow/PTI relationship and the trend of the A-D. All the technical "push" as shown by the PTI has produced is laggard performances (so far) in the Dow and the A-D. There is a limit to how far the PTI will rally "on its own."

ROT: Pity the poor investment advisor. Pity the crestfallen fund manager. Pity the public. Pity everyone connected with securities. Why, why should we pity all those well-meaning gentlemen and women? Consider this: according to A. G. Becker over the last ten years a portfolio all in stocks would have given a total return of 3.2%, a portfolio all in bonds would have provided a total return of 5.8%, while a portfolio totally in Treasury bills would have given you a total return of 6%.

So look at the accompanying chart. What it shows is that the institutions have turned negative on stocks. For instance, private pension plans in 1972 were selling off other assets to buy common stocks–as well as putting all of their new money into common stocks. From 120% investment in stocks in 1972, the pension funds have dropped to about 12% today.



What's happening? The bitter fact is that neither common stocks nor bonds are keeping up with inflation. Where is the money going? It is going increasingly into NON-PRODUCTIVE assets such as stamps, coins, art, collectibles, and yes–real estate. A fund buys a building yielding 8%, and at least the fund can boost the rents and in that way keep up with inflation. Furthermore, rare stamps have increased about 19% a year over the last 10 years and many other collectibles have done equally as well.

With inflation now rampant in the US, we find ourselves following (as it seems we always do) Britain. Britain has taxation up to and over 90% of high income. Nobody saves money in Britain anymore, the government takes it all–and in return it gives you comfort, health care, guidance, warm milk. So the British say, "the hell with saving" and they go out and have a good time. London has become the "fun capital" of the world, while New York has become the escape hatch, the place to put money "just in case."

As matters are progressing in the US, it could be that we will see a long, drawn-out slide into lethargy and non-productiveness, with the Government deciding more and more and taking over more and more of the power that was once reserved for the US citizenry.

How can we turn it all around? I've said repeatedly that from where we are now it would take a depression to turn this nation around, a depression to knock wages and prices down to where we're competitive again, a depression to force Government out of private industry and down to a size where it isn't a burden on each and every citizen in the nation (that is, those who are not working for the Government).

As investors, what can we do to survive the dry rot of inflation or stagflation? There's only one way to deal with the situation that I know of–and that way is diversification. That means that it is desirable to own your own house, you might keep 10% of your assets in gold, perhaps another 20% in some form of collectibles such as stamps or coins or antique guns, and the rest in T-bills awaiting a chance to come into the stock market at an ADVANTAGEOUS spot.

Thus, Big Government, passivity, greed and inflation have made each and every one of us a victim. No longer (as during the 1930's, 40's and 50's) can a man or a woman buy an insurance policy or a bond or put money in the savings bank, then sit back and feel the richer for it. As I've said to many people, during the 1930's and '40's it was hard as hell to make a buck, but if you did and you could put it away, you had something. Now you can make lots of bucks, but you don't really trust anything or anyplace or any vehicle to retain that dollar's purchasing power. As a matter of fact, you can't even swear in 10 years that the dollar will be legal tender!

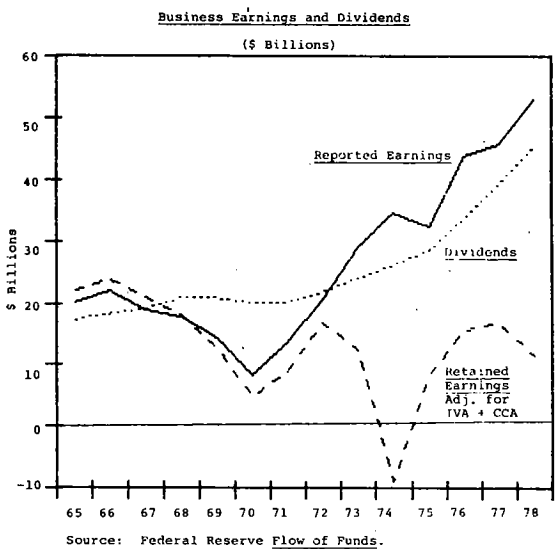
This rotting away of the fruits of men's labor is, to my mind, the single greatest cause of frustration and immorality in the US today. There is no one as angry or vengeful as a man who has seen his life's savings and his income stolen from him. Such a man sees himself as "an economic slave," no longer receiving the reward of his sweat and no longer in control of his own economic well-being. And that's where we are today. It's a situation which has to erupt somewhere ahead.

EARNINGS: Is the stock market crazy? Is the Dow only worth 7-8 times earnings? Are many stocks only worth 4 to 5 times earnings and is the Dow only worth 85% of book value? My answer is that the stock market adjusts for EVERYTHING, and that there may be two major factors that stocks are now discounting.

The first is that P/E ratios are always lower after four years of an economic boom. The reason is simple–after four years on the upside, the economy is four years closer to the next recession. And thus seasoned investors are offering less (in terms of P/E ratios) today than they did in late 1975 when the boom was just beginning.

Second factor: retained earnings for all (non-financial) US corporations rose to a record $52 billion in 1978 (see chart). This came after a fat $45 billion increase in 1977. However, it is estimated that 50% of all retained earnings came from inflation of inventories! On top of this depressing revelation, we must realize that depreciation is figured on the basis of historical rather than replacement costs.

According to Manufacturers Hanover Bank, when 1978's record undistributed profits (profits after dividends) are adjusted for inventory valuation and replacement cost depreciation, "what is actually left is a meager $11.3 billion or only 21% of the $52.7 billion that was reported in that period. Moreover, when this adjusted profit figure is further corrected for the loss of purchasing power of money, it becomes obvious that despite the strong rebound in current dollar terms, non-financial corporations were generating considerably less real earnings from operations last year than in any other year since the beginning of the present expansion. Which is hardly the sort of thing that nourishes capital spending."



As we study this chart of reported earnings vs. adjusted earnings, we realize these reported earnings could collapse if (1) the inflation rate declines, or (2) if the economy contracts. Also, since the dividend payout ratio is now fairly high, any decline in either inflation or the economy could bring on wholesale cuts in dividends throughout corporate America.

All this the stock market knows and understands. And that is why the current P/E ratio for the Dow is only 7.6, that's why the P/E for the Transportation Average is only 5.3, and that's why the P/E for the Standard & Poor's 500 Stock index is only 8.07. The fact is that the stock market just doesn't believe today's corporate earnings (even though analysts continue to repeat that "today's stock market is ridiculously cheap").

Question: Why don't the corporations go in for replacement accounting? Why are they so interested in putting out "phoney earnings reports?"

Answer: Because phoney earnings reports tend to push their stocks up. There's tremendous pressure to look good and get those stock quotes moving to higher levels. If you or I owned these same companies, we'd do everything we could to get expenses written off, and the lower the announced profits the better. That's the real, honest, conservative way of doing business. The unbelievable irony of the situation is that US corporations paid out an extra $32 billion in taxes on these unadjusted, phoney earnings. But that's what happens when men handle other people's money rather than their own!

Question: If gold and art and stamps and houses and all collectibles are now selling at prices that are adjusted for inflation (or let's say that are selling at replacement cost), why are stocks on average selling below replacement cost?

Answer: Collectibles and even houses and land, in these inflationary times, have literally become an alternate form of money. With all the markets now "hot," houses, land, coins, guns, etc. are being traded as if they were alternate forms of cash.

But the value of a stock is based on its ultimate earnings and payout ability. Nobody treasures and enjoys an IBM or a Control Data stock certificate. What the buyer really wants is a piece of IBM because he wants a piece of IBM's potential ability to earn money and provide a return. Thus, the potential return on IBM is what attracts the buyer of IBM stock, whereas the beauty, the rarity, the desirability of a diamond is what attracts the diamond investor. The minute you buy a diamond you've "got it all." An equity is not something you enjoy but is something which represents a *potential* return on invested capital.

NOTES & QUOTES: In answer to many inquiries, here are some liquid asset funds which I like. *Capital Preservation* (100% invested in Government short-term paper), 459 Hamilton Ave., Palo Alto, CA 94301. Cap. Pres. average yield about 8.8%..... *Fidelity Daily Income* (51% CD's, 26% Bankers Accept., 22% Comm. Paper) 82 Devonshire St., Boston Mass. 02109 (approx. 10.1% return). . . . *Price Prime Reserve* (21% CD's, 38% Comm. Paper, 28% Euro. CD's), 100 E. Pratt St., Baltimore, MD 02110 (9.84% return).

Of 12 leading no-load tax exempt bond funds, not one of them provided a total return (yield plus appreciation) of as much as 3%, while 9 out of the 12 provided losses on a one year basis (Mar. 30, 1978 to Mar. 30, 1979). On a current yield basis (forgetting fluctuations in price) Fidelity High Yield Muni Fund provides the highest yield at 6.65% (although these are not highest quality bonds) while Dreyfuss Tax Exempt provides second higher at 6.6%.

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Have you read about the monster entertainers' salaries at Las Vegas. They are huge, in many cases, but it's not all gravy. Here's what Joan Rivers said about her $55,000 per week Vegas salary (from *Money* Magazine):

> *Las Vegas is as famous for its big salaries as for its slot machines. How much of that $55,000 a week do you get to keep?*
>
> Off the top there's 15% to the manager, 10% to the agent, 5% to the business manager, 5% for publicity—and 50% of the rest in taxes. Then there are expenses: travel, costumes that cost you a fortune, tips—tips backstage, front stage, room service, thank you very much. Each group has a kitty for tips. And the hotel telephone operators. There are 73 hotel operators at the MGM Grand Hotel. And your life is your phone. When the bellman brings you flowers and you give him $2, he wants to spit in your face because he just read where Sinatra gave somebody $400. So the rule of thumb is you get to keep 20%, but as you can see it isn't even that.

* *

Peggy Guggenheim of the great copper fortune now lives in Venice at age 80. Her biography will be coming out in October. She was one of the early and original collectors of "modern art" during the 1930's. As a hobby she ran an art gallery in Paris prior to WW II, exhibiting such masters as Picasso, Calder, Kandinsky, Duchamp, Arp, Brancusi. Their avant-garde art would not sell, so Peggy would buy a painting at each artist's showing to "encourage" him. She estimates that she spent about $40,000 on such art purchases during the '30's. When the War broke out she asked the Louvre to help her get the paintings out of Europe, but that famous museum didn't think her collection was worth the effort. Estimate market value of those paintings today: $30 million. It is a fact that some of the great fortunes have been garnered by people who held on to their collections just because they loved them and could not bear to part with them (regardless of market value). Many invaluable stamp and coin collections have been built the same way.

* *

Howard Ruff's new book, "How to Prosper During the Coming Bad Years" is (fantastic) the fourth best selling book in the nation today. I believe that Howard together with Harry Browne and Jim Blanchard have probably done more towards alerting the American public to the dangers of inflation and the course that this Government is taking than anyone else alive. It ain't just what you say–it's whether you say it loud enough and whether people understand what you're saying.

* *

I want to thank the American Economic Council for awarding Dow Theory Letters the "Liberty Award" for the "most outstanding Market Letter in 1978." The Council sent me a very pretty silver cup, which, I take it, is more than just an inflation hedge.

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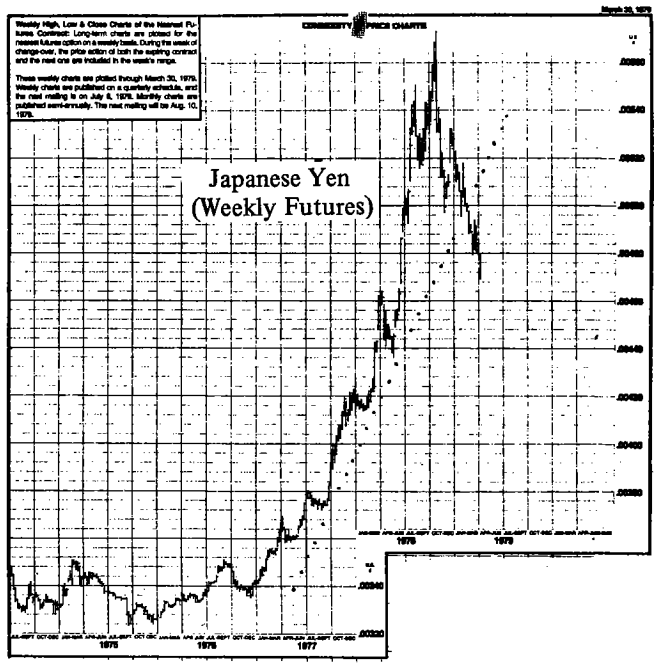
You've probably heard all kinds of rumors and chatter about the dangers of being elected President in 1980. You may not believe in cycles, but here are the strange facts. Over the past 139 years, every President elected in a year ending in zero has died or been assassinated in office. 1840, Harrison elected, died (1841) in office. 1860, Lincoln elected for first time, assassinated in 1865. 1880, Garfield elected, assassinated in 1881. 1900, McKinley elected to 2nd term, assassinated in 1901. 1920, Harding elected, dies mysteriously in 1923. 1940, Roosevelt elected to third term, dies in his fourth term in 1945. 1960, Kennedy elected, shot in 1963. 1980 . . . . .



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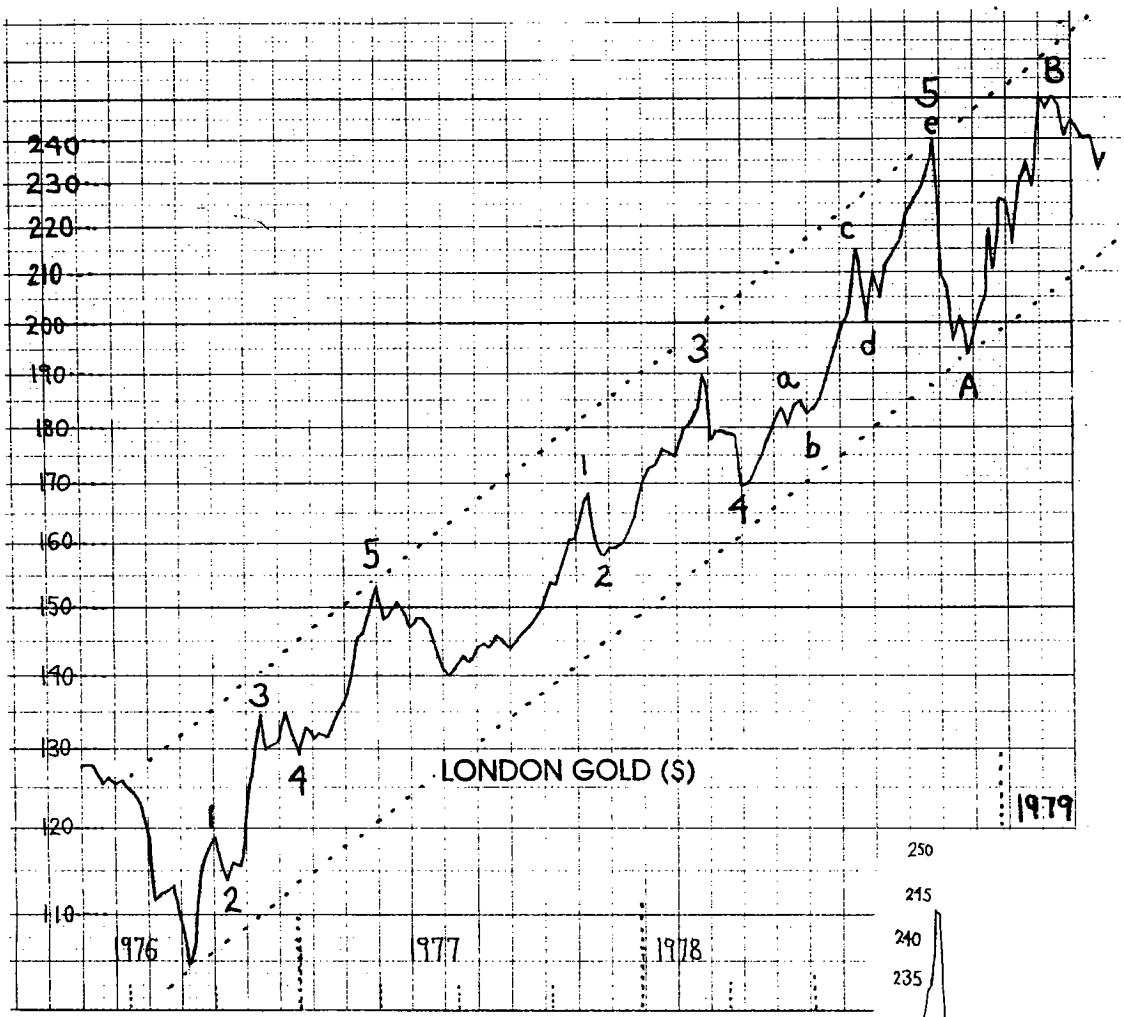
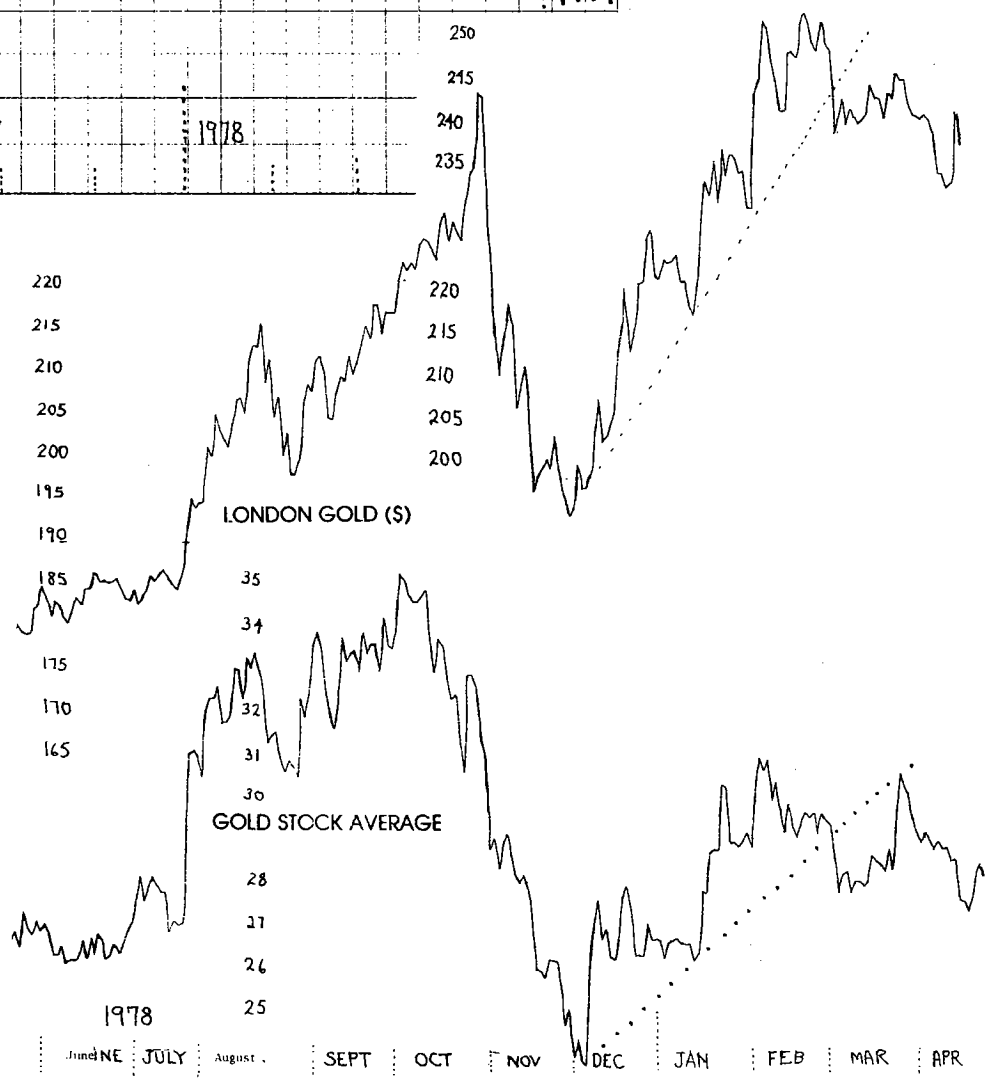
This weekly chart of the Japanese Yen (courtesy of Commodity Price Charts) shows the yen cracking wide against the dollar. I suggested that traders short the yen a few months ago. The projected Japanese deficit is going to be about $80 billion, equal to $160 billion on a comparable GNP basis with the US. The dollar is now going up against both gold and the "hard currencies." I said this at the turn of the year, and I'll say it again: The dollar is experiencing a big bear market rally, not a primary rise. But the rally is now amazing everyone (as I thought it would), and it should go on for a while longer.

GOLD: On page 7 I show my ratio chart of gold starting from the 103 low of August 1976. I have all along pictured the move in gold in terms of the Elliott Wave thesis, and I believe this analysis is still valid (although it has been misinterpreted and mangled by many analysts).

The first phase of gold took the metal to just above 150 in early 1977. This phase traced out a 1-2-3-4-5 pattern. A mild correction took gold back to the 140 area. The next phase took gold to 243 in late-1978, and here again we saw the bull move follow at a 1-2-3-4-5 rising pattern. The 5th wave of this pattern extended, and I show this with an a-b-c-d-e on the chart. Extensions are never the end of a move, but they are often followed by good corrections.

Gold broke to 193 in November, 1978 (A on chart). Then with the help of all kinds and varieties of political crises, gold rose (actually above the previous high) to point B on the chart–to 253. From there gold turned down again, and that's where we find gold now–having backed off to the 236-239 area, and still in a corrective phase.





I have drawn all the gold action since August, 1976 as having taken place within a major rising channel. It will be crucial from this point on to note whether any remaining corrective action holds within the channel–or whether the channel is ruptured. The bottom of the channel is now at about 220, so this is the level that I would term critical. If 220 is broken, I would expect gold to test 200 and probably test the 193 level at A again. But if 220 holds, then it is probable that gold is nearing the end of the correction, and accumulation of gold will again be in order.

I would say that it is a plus for gold that at B the price level had enough power to better the 243 level–despite the fact that a major correction was in progress. But the lower channel line still holds the important clue as to the strength of gold, and we should see this test completed before 1979 is over.

The second chart shows daily London gold (2nd fix) together with my gold stock average (GSA) plotted daily.

As a rule, valid movements are confirmed by *both* gold and the GSA. The GSA during January and February stubbornly refused to confirm the new high in gold. In early March gold broke its rising trendline, confirmed by a break in the trendline of GSA. Last week, even after the announcement of a 50% cut in the amount of gold coming to US auctions, the action of gold was unimpressive.

This chart tells us that the trend of the gold complex is still down. Too many weak hands have moved into the precious metals picture, but with each successive decline, stronger hands tend to accumulate. Somewhere ahead the third and final phase of the gold bull market will materialize. That should be something to behold–but the time is not yet, not yet.

LATE NOTES: For my moving averages of the Dow study, I now use "front-weighted" moving averages, and these tend to be more sensitive and provide earlier cross-over signals. On March 9 the 13-week moving average (MA) of the Dow crossed above the 50-week MA. The cross-over took place with the actual Dow at 842. Since I did not consider this signal a primary bull signal, I did not make a big fuss of it.

A month has now passed and the Dow is only 13 points above its price at the "bullish cross-over." I consider that a poor performance. The 4-week front-weighted MA of the Dow is now at 865, the 13-week MA is at 849 while the 50-week is at 838.

New highs on the NYSE (52-week basis) hit a peak of 80 on April 11 (using a 5-day moving average). That's a very weak performance and hardly suggests a big move coming up in the majority of NYSE issues. In other words, in four months of rallying in 1979, the best we got was a 5-day average of 80 new highs. Not good.

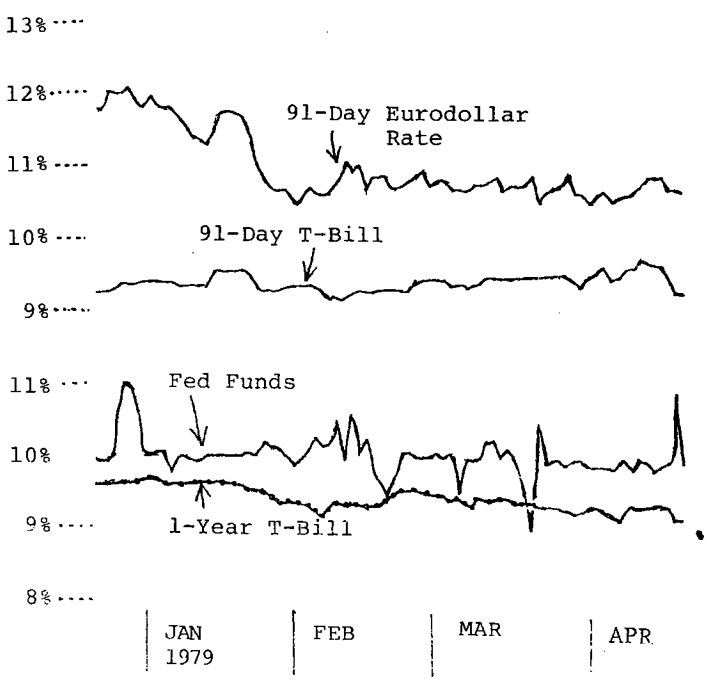
Ned Davis notes that his specialist short ratio is not at 84%. This high level on the ratio (5-week basis) has never **failed** to touch off a selling spree in the market. The average drop for the Dow for all the previous sell signals on the specialist short ratio was 15%.

* *

Last week short-term interest rates fell with the yield on the 91-day T-bills hitting around 9.20%. But the long end of the bond scale fell too. The D-J 20 Bond Average hit 84.12, lowest level since late-1975! The long-term Treasury bonds are all yielding over 9% with many of these issues dropping last week to all-time record lows. Analysis: we're seeing big institutional interest in short-term credit instruments, but we're also seeing increasing fear of "perpetual inflation" and an ever-sinking long-term bond market. It should be remembered that a sliding bond market provides a very unstable and negative background for stocks.

* *

Wall Street has moved to the edge of its "financial chair" with anxiety and anticipation over the money rate game. I show here my chart of four telltale short-term interest rate indices. The trend on all four would seem neutral to slightly lower. If the Fed is putting the squeeze to the money market, you sure can't detect it from this chart. BUT, that trend to new lows in the long term bond market is ominous. Long-term bonds are still in active competition for money, and at some point rising long-term rates become irresistible.



NEXT MAILING: May 9th

The Wizard may just have made the ultimate comment about inflation. Unless it was Jimmy Carter, who now tells us that everything bad on the face of the earth is the fault of the big oil companies and their obscene profits.